

Supply chain management at nicholas piramal india



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Supply Chain Management at Nicholas Piramal India Case Study Noemie Bisserbie, ET Intelligence Group, Oct-Nov 2006 Supply chain management (SCM) is one of the leading cost saving and revenue enhancement strategies in use today. Pharmaceutical companies are increasingly using this technique to improve the entire functional process.

SCM has also helped companies enhance their efficiency in managing resources and improving relationships. In the case of Nicholas Piramal, SCM has proved to be one of the most powerful engines of business transformation. Since the company's decision to enter the high growth contract manufacturing and research services (CRAMS) segment, SCM has become key to the company's strategy. After the acquisition of Avecia (UK) in 2005, and more recently, Pfizer's UK Morepeth facility, the company's ability to integrate over seas businesses and ramp up of supplies becomes key to the profitability it's CRAMS business.

Background Three years ago, India's fourth largest pharmaceutical company, NPIL, came up with a total restructure plan. Post patent regime, the company identified CRAMS as a major growth opportunity. With a slowdown in patented drugs sales and drying R&D pipelines, global pharmaceutical companies are increasingly exploring low cost options for outsourcing research and manufacturing. According to industry sources, the global pharmaceutical outsourcing market, which currently stands at \$24 billion, could reach \$53 billion by 2010. Low cost manpower and a large base of FDA approved plants, positions India high on the outsourcing list, Seven Lifesciences, GVK Biosciences, Jubilant Organosys, Nicholas Piramal and

Shasun Chemicals & Drugs now featuring among the leading Indian players in this segment.

Custom manufacturing for innovator companies stands out as the most attractive outsourcing opportunity for pharma companies. This market could reach, from an estimated \$16 billion today, to \$25.7 billion by 2010. With the largest number of FDA approved plants after the US, India could potentially capture 10% of this opportunity. Change was inevitable. Within just three years, NPIL has changed its entire business model.

NPIL's recent buyout of Pfizer's Morpeth facility, puts it on top of the league of Indian contract manufacturers with expected annual revenues of Rs 900 crore. While its international business accounted for just 3% of revenues in 2002-03, today it represents 50% of NPIL's business, while domestic revenues account for the remaining 50%. SCM has played a crucial part in this transition. Since its decision in 2003 to enter the contract manufacturing business, NPIL has invested close to \$175 million (Rs 806 crore) towards creating capacity in the segment. The company has spent about \$100m on greenfield projects in India, and paid up around \$25m and \$50m towards the acquisition of Avecia and Pfizer's Morepeth facilities, respectively.

The acquisition of Pfizer's Morpeth facility is a big win for NPIL, as it fulfils its search for a significant acquisition in the contract manufacturing space. The facility comes with a five - year supply contract that could yield revenues of \$350 million (Rs 1610 crore) during the tenure. The domestic company also expects to tie up with new customers. Morepeth's base in Western Europe could enhance its appeal with other global pharmaceutical companies who

may be more comfortable about sourcing from a UK-based plant. NPIL is confident that the track record of the company should help it attract new customers. While Nicholas Piramal's acquisitions have allowed the company to build a critical mass and increase its technology range, the company will need to rationalize costs by synchronizing operations with the Indian assets and by sourcing intermediates from new locations to make the Avecia and Morpeth businesses competitive.

NPIL is notably looking at China as an opportunity to reduce sourcing costs significantly. Through these means, NPIL expects to cut costs by as much as 30%. Avecia sourced intermediates from Europe, notably Italy. The increase in topline as well as higher productivity combined with an integration with the Indian operations, should allow Avecia to breakeven by the end of this year. In case of Morepeth's facility, NPIL is not looking at major restructuring but synergies with Indian operations should make the facility more profitable.

Notwithstanding the global foray, NPIL's strategy should not be construed as a move to reduce its focus on the domestic market. India remains the core of its strategy. Domestic formulations market will continue to drive overall margins and provide a strong cash flow for the contract manufacturing business and for research. NPIL continues to upgrade its research and development facility and its talent base in order to meet the needs of its contract research business. Going forward, NPIL will look at both inorganic and organic growth in order to increase its product portfolio, as well as its technology range.

To fund future acquisitions, the board has approved a resolution to raise up to \$1bn (Rs 4, 608 crore), through the issue of securities in the domestic or international markets. While the company is not looking at a major acquisition, it could complete small to medium takeovers, if the opportunities arise. Investments in contract manufacturing have affected the company's profitability in the short term, but margins are set to increase as revenues from its CRAMS business start flowing in. Integrating the Avecia and Morpeth businesses, acquired in the last year and ramping up supplies is expected to be the key to profitability. SCM has and will continue to play a crucial part in this transition.

Challenges for SCM at NPIL Today, NPIL faces three major challenges in order to integrate its Indian and international businesses. The first challenge is cultural. Integrating cultures across India, Canada and UK has not proved easy. NPIL has found itself confronted to ego issues, senior executives in UK subsidiaries finding it difficult to report to Indian managers, as well as communication problems.

Sharing data between NPIL's newly acquired business entities has also sometimes proved difficult. In the midst of changes, the company cannot stick to one rigid system. Sourcing and manufacturing will be another issue supply management executives will need to look close at. NPIL will need to change its sourcing locations for its Avecia business. China's conscious effort to increase the quality of its bulk drugs makes it an attractive sourcing location. For certain formulations, Chinese manufacturers can offer one-tenth the price offered by European manufacturers.

There are however a few drawbacks. The Chinese Government has reduced export subsidies, manufacturing facilities are affected by an increasing number of power hortages and are becoming more environment conscious. As a result, many industries are shutting down. However, competition has constrained European suppliers to considerably reduce prices and NPIL has significantly benefited from this opportunity. In India too, by synchronizing operations between its four domestic manufacturing facilities, the company expects to reduce costs by 5% to 10%.

Reducing sourcing costs will be crucial to the success of the company's foray into CRAMS, as it will largely determine the business' profitability. While NPIL is already one of the most established players on the domestic market, transportation and goods inventory management are two areas the company is trying to further improve. SCM will need to continue to drive significant changes on the domestic market as well, which still account for a sizeable chunk of the company's revenues. Besides, while CRAMS is set to account for close to 80% of revenues on the medium to long term, NPIL's domestic formulations is expected to remain more profitable than the company's international business. In spite of last year's deluge bad memories, no major changes have been implemented in finished goods inventory management.

Finished goods inventory continues to remain deliberately high. However, on the material side, NPIL has implemented new systems to reduce inventories. NPIL has 28 depots and spends 8 lakhs to 10 lakhs in information communication. This has proved productive, as the company has been able within six months to reduce materials inventory from 40% to 25%, which is

much lower than the industry's average. NPIL is the only company in the industry to have a separate force for stockists.

While in most pharma companies, medical representatives are also in charge of looking at stocks, at NPIL, a dedicated team of 200 people are solely responsible for keeping an eye on stocks and booking orders for the company. The next challenge will be to connect stockists directly. This is a step most FMCG companies, such as HLL, have already taken, but NPIL is the first mover in the pharmaceutical industry. The main reason is that while stockists in the FMCG sector are dedicated to one specific sector, there is no clear demarking of territories for pharma stockists, which are organized in strong associations. Besides, focus on logistics is not very high as it represents a small share of sales.

However, NPIL is starting to implement systems, which most companies considered unfeasible in the pharma sector. On the supply side, while NPIL used to deliberately source materials from a reasonable number of suppliers because of the risks of strikes, the company has shifted to a single window. This has allowed the company to gain in bargaining power and reduce prices by 5% to 10%. Finally, the company has reduced the number of transporters in order to improve the quality of services and diminish delivery time. Metros remain the main market in India.

Although this move has led as expected to a clear improvement in terms of quality, it has considerably increased transportation costs as well. Finally, while it has not traditionally played a major role in the pharmaceutical sector, as domestic companies get a global foot print and enter new

segments, SCM is becoming key to pharma companies' entire business model. In the case of NPIL, SCM has proved to be the company's engine to growth. NPIL's ability to turn around foreign businesses will be key to the success of the company's foray into CRAMS.